Distr.
GENERAL

UNCTAD/PA/6
6 June 1994

ENGLISH ONLY

STANDING COMMITTEE ON POVERTY ALLEVIATION
Second session
Geneva, 25 July 1994

Item 4 of the provisional agenda

EFFECTS ON POVERTY ALLEVIATION OF STRUCTURAL ADJUSTMENT PROGRAMMES, JOB CREATION POLICIES, AND MEANS FOR THE PARTICIPATION OF SMALL-SCALE AND MICRO-ENTERPRISES IN INTERNATIONAL TRADE

The role of small and micro-enterprises in poverty alleviation through participation in international trade

Background note by the UNCTAD secretariat

GE.94-52436

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EXECUTIVE SUMMARY

1. This note assesses the export potential of the small-scale sector in the developing countries with emphasis on the issue of employment creation for the poor. A number of policies are proposed which could be instrumental in easing the main constraints on the sector's capability to expand exports.

2. The small-scale sector has been defined as enterprises employing up to 50 persons and operating in rural and urban non-agricultural activities. However, the sector is far from being homogeneous. In terms of responsiveness to government policies, a distinction can be made between formal and informal sector enterprises. The main implication of the different legal status of enterprises is that, in practice, the informal sector cannot generally be reached and assisted by standard government policies designed for the formal sector.

3. Shrinking employment opportunities in the large-scale sector, especially public sector enterprises, have refocused the attention of policymakers on the small-scale sector and its contribution to gainful employment. Its high capacity to absorb labour, low skill requirements and use of labour-intensive techniques have been pointed out as being well-suited for generating employment for the poor.

4. Low demand in the domestic market of the developing countries has also given rise to the question of the possibilities of small-scale enterprises in the export sector. Even if most of them lack the capacity to export, there is a considerable untapped export potential within the sector. The small-scale sector's competitive edge is in low prices resulting from low labour costs, flexibility and ability to fill small orders or produce small quantities of products. Three types of enterprise can be reasonably supposed to have good export prospects: (a) small formal enterprises engaged in standardized manufactures' production, (b) micro-enterprises operating in handicrafts, and (c) micro- and small informal enterprises involved in making standardized products through, *inter alia*, subcontracting from larger enterprises.

5. The small-scale sector's performance in international trade has been adversely affected by a number of problems. Two types of constraints can be identified: (i) the constraints that are internal to the small-scale sector enterprises themselves and which result from the lack of entrepreneurial capability and skills, from the low quality of products, etc.; and (ii) the constraints that are external to this sector, namely unfavourable national policies and protectionist measures reducing access to export markets.

6. The main scope for government policy measures appears to be in providing not only durable macroeconomic policies but also direct support measures to this sector. Employment-inducive and at the same time export-promoting growth strategy may eliminate the anti-export bias and facilitate the participation of the small-scale sector in international trade. The recent wave of trade policy reforms introduced by many developing countries in the 1980s is an important step in this direction. Available studies show a rise in export performance in the late 1980s, in particular in labour-intensive manufactures largely produced by the small- and medium-scale sectors.

7. Measures targeted to support the small-scale sector in international trade are needed in addition to the use of macroeconomic instruments. Direct measures that could be adopted include: (i) strengthening the export marketing capability of the sector (through, for example, assistance in quality control; access to appropriate technologies, packaging and marketing; provision of training courses etc.), and (ii) facilitating access to credit for small-scale activities. In analysing government measures in this field, however, an important fact to be kept in mind is that there is scope for the small sector to assist itself (e.g. through professional associations), and for foreign partners (customers) to help in upgrading the small-scale sector's export potential.

8. Improved access to developed countries' markets is another issue, which is crucial for the success of small-scale sector exports. Concerns about rising unemployment in most developed countries do not facilitate the efforts required for easier access of labour-intensive products from developing countries. Despite existing problems, however, these efforts should continue to be pursued. Diversification of exports - from traditional and sometimes sensitive items to non-traditional products less vulnerable to protectionism - would also be an option for developing countries in this case. The ideal would be, however, to work towards achieving balanced trade in the framework of increasing interdependence between developed and developing countries.

INTRODUCTION

9. The important role that can be played by the small-scale sector in alleviating poverty has been singled out because of its potential to generate employment and income for the poor. Deteriorating economic conditions in the developing countries since the beginning of the 1980s have directed attention to the possibility of expanding employment creation opportunities by this sector through export-oriented activities.

10. This note addresses the question of employment creation for the poor through greater participation by the small-scale sector in international trade. Its main objectives are: (a) to assess the small-scale sector's export potential; (b) to identify the types of enterprise that are likely to succeed in international markets; (c) to analyse the major constraints facing export-oriented enterprises; and (d) to discuss the policies that may improve the sector's export record and create new employment opportunities. Some policy measures are suggested at the end of this study.

I. POTENTIAL OF THE SMALL-SCALE SECTOR FOR EMPLOYMENT CREATION AND EXPORTS

A. Basic concept of the small-scale sector

11. The small-scale sector is generally understood to mean those enterprises employing up to 50 persons and operating in rural and urban non-agricultural activities, for example, in manufacturing and services. However, this particular definition is rarely reflected in statistical data. Small-scale enterprises are frequently grouped together with medium-sized enterprises (i.e. those employing from 51 to 100 persons) under the label of small and medium-sized enterprises (SMEs).

12. In order to understand better both the advantages and the constraints facing small-scale enterprises we begin the discussion in this section with a classification of the small-scale sector. Two types of classification seem to be relevant for the purpose of this study, namely (a) according to the size of an enterprise, and (b) according to the legal status of an enterprise.

13. With respect to the first classification in which size is the decisive criterion, two groups of enterprises can be distinguished: (a) **micro-enterprises** employing between 2 and 10 persons (this category also includes self-employed individuals who constitute the overwhelming majority), and (b) **small enterprises**: employing between 11 and 50 people.[1/]

14. A number of other differences between the micro- and small enterprises can be identified, although sometimes the dividing line is not completely clear. Table 1 below gives some of the salient features of micro- and small enterprises.

Table 1

Differences between small and micro-enterprises

Criteria	Micro-enterprises	Small-scale firms
Employment structure	Owner and family members	Employment of workers in addition to owners.
Education	High percentage of illiterate (especially among women), mostly "on-the-job" training.	Longer formal schooling; more frequent formal training.
Financial resources	Mostly internal (personal savings, family sources) or reliance on money lenders	Use own resources but to some extent also formal (external) resources.
Rural/urban setting	House, backyard, open air	Regular workshops.
Use of public services (water, electricity, telephone)	Very rare	More frequent.
Inputs	Locally-available and often recycled	Higher proportion of imported inputs.
Technology	Mostly traditional; use of hand tools, high labour-intensity	Often modern, upgraded, use of machines.
Products	Low quality, rough finishing	More attention to quality and packaging.
Markets	Mostly low-income local consumers, medium to large enterprises	Local low- and middle-income consumers, some larger enterprises and export markets

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1/ Data collected by Liedholm and Mead (C. Liedholm and D. Mead: *Small-scale Industries in Developing Countries - Empirical Evidence and Policy Implications*, USAID, Washington, D.C., 1986) on industrial employment demonstrate that the bulk of jobs is provided by micro-enterprises (for example, 83 per cent in Zambia, 1985, 66 per cent in the Philippines, 1974, 65 per cent in Vanuatu, 1990).

15. In terms of policy considerations, the second classification seems to be crucial, namely the division of small-scale enterprises according to their **legal status** into formal and informal sectors: **formal sector** enterprises are registered with the authorities, whereas the **informal sector**[2/] enterprises are not; they are therefore not legally recognized and hence are officially non-existent. Nearly all micro-enterprises, and some small enterprises as well, fall into this category. In fact, each of these sectors tends to operate in a fundamentally different legal setting which determines its responsiveness to government policies. Major differences between the two sectors are summarized below in table 2, with an assessment of the advantages (indicated by +) and disadvantages (as -) which any particular component of formality/informality brings to enterprise competitivity.

Table 2

Advantages/disadvantages of formality/informality

	Informal sector enterprises		**Formal sector enterprises**
+	Do not pay taxes	-	Pay taxes (depending, however, on the enforcement capacity of the government).
+	Are not subject to government regulation (especially in terms of labour legislation, such as minimum wages)	-	Have to comply with government regulations.
-	Unable to use formal institutions such as banks, marketing boards, training facilities, etc.	+	Able to contact formal institutions (apply for bank loans, premises, electricity).
-	Unable to profit from government assistance	+	Have access to government assistance schemes, both general and those designed for small-scale sector (concessional finance and services, tax allowances, etc.).
-	Cannot export and import on their own. Usually need the intervention of intermediaries.	+	Can carry out foreign trade operations on their own.
-	Have no influence on government policies as they are not organized.	+	May be able to exercise some pressure on government (through professional associations).

2/ According to estimates (OECD, *Development Co-operation - 1991 Report* (Paris, 1991) p. 70) the informal sector accounts for between 30 and 70 per cent of the economically active population in the developing countries (its share is over 60 per cent of the labour force in Africa, from 50 to 75 per cent in Latin America, and from 10 to 20 per cent in the NICs in East and South-East Asia (Economic and Social Council, *World Summit for Social Development*, Report of the Secretary General (E/1993/77), 1993, p.19).

16. Contrary to general expectations, most informal enterprises tend not to grow into formal ones. This is due to a set of complex social, political and economic reasons, such as the lack of potential for development (e.g. due to an inability to accumulate capital or to the lack of motivation to become formal because the advantages of informality may, in the entrepreneurs' perception, outweigh the disadvantages). In some cases, enterprises may well opt to remain informal for fear of losing their competitive edge in well-established or "niche" markets.

B. Potential of the small-scale sector for employment creation

17. The economic policy of many developing countries has long been based on the belief that rapid development could best be achieved by emulating what were perceived to be the industrial structures of the developed countries, i.e. structures based on capital-intensive large-scale industries. By the mid-1970s, however, this strategy was increasingly questioned as a result of the poor performance of these industries and the protection awarded to them. Large enterprises, in both the private and public sectors, which operated in a protected environment, often proved to be inefficient. In addition, the employment-creation objectives vested in them were rarely achieved.[y] This was largely due to their economies of scale and government policies that encouraged capital-intensive patterns of production.

18. For these reasons, it is now widely recognized that the large sector will, in principle, be unable to generate sufficient employment for the expanding labour force in developing countries. In this context, the small-scale sector is being viewed as a means to mitigate the employment crisis and to promote more equitable distribution of income. There are three reasons for this point of view. First, while, in developing countries, medium- and large-scale enterprises dominate in terms of value added, the small-scale sector leads in the share of persons employed. Second, it shows higher capacity to absorb additional and dismissed workers. Thus it offers a valid alternative to the shrinking opportunities available in the large-scale sector during recession and structural adjustment. Third, low-skill requirements and the use of labour-intensive techniques make the small-scale sector particularly well-placed for employing the growing numbers of the poor.

C. Export potential of the small-scale sector

19. The small-scale sector has been drawing increased attention because of its employment-generating capacity. However, any increase in production (and employment) in this sector is seriously hampered by what the entrepreneurs themselves identify as a main constraint to the development of their activities -

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[y] See, C. Liedholm and D. Mead, *Small-scale Industries in Developing Countries - Empirical Evidence and Policy Implications*, MSU International Paper No.9, Michigan State University, East Lansing, Michigan, 1987. Some argue, however, that higher labour intensity cannot be automatically identified with the small-scale sector. According to them, the size of the enterprise apparently proves to be irrelevant and what really matters is the technology employed. (W. Elkan, *Policy for Small-scale Industry - A Critique*, Background Paper for the *1987 World Development Report.*)

i.e. the problem of insufficient demand in the domestic market.[4] In this context, a possible strategy may be to exploit the potential competitive advantage of small-scale producers from developing countries and to export their products to developed-country markets,[5] thus augmenting production by selling both in foreign as well as domestic markets.

20. In order to assess the feasibility of such an approach, it is useful to examine the various factors behind the small-scale sector's competitiveness, to evaluate their relevance for its export capability, and to identify those enterprises within the small-scale sector that would have the potential to export successfully.

21. The main factors behind the small-scale sector's competitiveness and their impact on the capability to export are summarized in table 3 below:

Table 3

Factors contributing to the small-scale sector's international competitiveness

Factor	Relevance to international competitiveness
Greater flexibility (than larger units)	Yes.
Production of small sets of products	Partly, particularly for those with labour-intensive technologies.
Use of domestic resources	Partly, if they are cheaper than imported resources.
Use of traditional skills	Partly, if they are needed for the production of specific items, such as handicrafts.
Proximity to markets	No.
Low prices resulting from low labour costs	Yes.

22. In terms of international competitiveness, two of the above-mentioned factors are particularly relevant, namely the low prices of the finished products and the greater flexibility of small-scale sector enterprises. The latter is particularly important in determining competition in international markets. Yet, many policymakers still hold that the small-scale sector's competitiveness is

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[4] However, recent developments (real devaluations resulting in an increase in prices of importables) seem to boost the demand for the small-scale sector's products and services. More opportunities have appeared in (a) repairs and maintenance of ageing imported consumer durables and plant equipment and in (b) the substitution of simple tools and appliances or consumer goods produced locally for those that used to be imported.

[5] As available evidence on export possibilities in other developing countries' markets for labour-intensive goods made by small-scale producers is very scarce, this note will focus exclusively on access to developed countries' markets.

due to low prices resulting from low labour costs.[6] The best prospects for exports are therefore to be seen in **low-skill, domestic-resource-based and labour-intensive products.**[7] Based on factor content in goods, the most appropriate categories in terms of job creation (i.e. for unskilled labour-intensive products) and export prospects are textiles, clothing, leather, footwear, wood and cork, furniture and fixtures, printing and publishing, some pottery and glass products, some metal and non-metallic products, and food products.[8]

23. Any assessment of the small-scale sector's export potential has to take into account the fact that the majority of enterprises will never be able to participate in international trade. Two reasons can be mentioned in support of this statement. First, available case studies in the informal sector[9] show that approximately 75 per cent of those employed in this sector work in services (for example, as messengers, street vendors, servants, rickshaw drivers, shoeshine boys, etc.). Despite the fact that they represent jobs, such activities have no export potential. Second, a large proportion of manufacturers produce cheap, low quality goods that substitute for more sophisticated items produced by the formal sector or imported from abroad. Such goods attract few, if any, customers in the developed world, where the level of consumption is higher.

24. Despite the fact that the small-scale sector's export potential is limited, there are certain types of enterprise that have good prospects in international markets.[10] Three groups can be identified:

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[6] As a matter of fact, there is a substantial difference between developed and developing countries as regards labour costs in labour-intensive industries, which puts producers from developing countries in a good competitive position for exports. According to UNIDO data (calculated on the basis of UNIDO, *Handbook of Industrial Statistics, 1992*, p.38), labour costs (wages per employee per annum) were on average 4.5 times lower in developing countries than in the developed part of the world in 1988 in the food industry (20 times lower in Bangladesh, India, Indonesia, Sri Lanka and Malawi), 4 times lower in textiles, wearing apparel, leather products and footwear, 5.3 times lower in wood and cork products, plastics and pottery. However, the cost advantage in favour of developing countries is partially offset by the lower quality of the products and by the inverse difference in productivity. UNIDO data suggest that the value added per employee per annum is up to three times higher in developed than in the developing countries throughout labour-intensive manufacturing industries.

[7] However, new technologies are increasingly challenging the "cheap labour" hypotheses of conventional theories about the international division of labour.

[8] See, F. Senses, "The nature and main characteristics of recent Turkish growth in export of manufactures", *The Developing Economies*, XXVII-1, p.33.

[9] H.-R. Hemmer, "On the economic analysis of the urban informal sector", *World Development*, No.10/1989, p.1544.

[10] The role of the small-scale sector in exports, though generally small or non-existent in most developing countries, has been growing in parts of Asia and, to a lesser extent, in Latin America. The areas where this is occurring consist mainly of (a) countries with an established or growing record in export orientation (e.g. Brazil, Chile, China, Hong Kong, Republic of Korea, Taiwan Province of China, etc.); (b) certain countries where foreign direct investment is substantial (e.g. China, Malaysia, Mauritius, Mexico, Singapore, Thailand, etc.), and (c) some cases of government-supported export efforts (e.g.India).

1. **Small modern enterprises (formal)**

25. These enterprises are able to profit from both low labour costs and generally higher technology and quality to be competitive in the production of standardized manufactured products or in subcontracts to larger enterprises. In these cases, more durable and regular relationships with customers are the rule. Country studies from Peru, Ghana, Mexico, India and Indonesia,[11] assessing the prospects of small-scale sector enterprises according to their size and technological background, provide support for the argument that the best prospects lie in particular with the relatively larger, technically more advanced and export-oriented enterprises.

2. **Micro-enterprises operating in handicrafts (informal)**

26. Low labour costs and the use of traditional skills are the main determinants of the micro-enterprises' competitiveness in handicrafts. A competitive price as well as the perception of these products by foreign customers as expressions of a particular culture and tradition have largely contributed to the success in expanding exports of clothing, leather products, wood carvings, carpets, metal work and jewellery by India, Sri Lanka, Kenya and others.

3. **Micro- and small enterprises engaged in standardized production (informal)**

27. New prospects appear to have opened up for informal enterprises as a result of growing competition in international markets, leading to more flexible patterns of production (smaller orders, just-in-time deliveries) and the search for reduced costs. "Putting-out" systems are frequently used: micro-enterprises become subcontracted labour-intensive operations (for example in the garment or footwear industries). Orders are placed by large enterprises, including multinationals, but only after export contracts have been concluded. This pattern of relationship increases the flexibility of large enterprises and, of course, cuts costs.

28. While it is true that small and micro-enterprises' export efforts are frequently hampered because they are too small, and hence unable to operate efficiently to reach foreign markets on their own, there has been a growing trend for small units to increase their competitiveness by creating **industrial clusters**. Similar in some aspects to the Italian model of industrial districts, these clusters have performed very well in a number of developing countries (e.g. Brazil, India, Indonesia, Kenya, Peru, Republic of Korea, Rwanda and others[12]). Small enterprises, in such circumstances, have tended to organize business networks of geographically concentrated firms operating in a specific industrial sector. The firms are linked with each other through subcontracting arrangements and a set of common social links and values. These industrial clusters have proved very useful in fostering competitiveness. In particular, they have

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[11] Cited in K. Nadvi, "Industrial district experiences in developing countries", Background Paper for the UNCTAD/GTZ symposium on "The Role of Industrial Districts in the Application, Adaptation and Diffusion of Technology", Geneva, 1992.

[12] For details, see, for example, K. Nadvi, *op.cit.*, or H. Smitz, *Small Enterprises and Fordist Giants - Tale of a Supercluster*, Discussion Paper No.331, Institute of Development Studies, 1993.

greatly facilitated: (a) the loan or renting of tools and equipment, (b) subcontracting to neighbours when a large order is secured, (c) sharing general information on new or improved products and technology (yet keeping specific information for themselves and competing with each other), and (d) attracting customers as a result of the concentration of similar activities in close proximity.

II. MACROECONOMIC MEASURES TO SUPPORT THE SMALL-SCALE SECTOR IN INTERNATIONAL TRADE

29. The small-scale sector's record in general, and in international trade in particular, depends largely on the presence of economic growth and on the type of growth strategy adopted. Economic growth creates new markets and the growth strategy determines the basis of this growth, including the kinds of technologies, markets and enterprises that are encouraged.

30. Recent experience suggests that macroeconomic policy is crucial for the long-term and viable development of the small-scale sector. It is argued[13] that indirect macropolicy interventions may do more to promote small industries than the direct measures prevailing in the past. This view is based on the assumption that entrepreneurs will respond better to market signals, particularly if market failures are redressed. Despite the limited empirical evidence on this issue, an attempt is made below to assess the impact of macroeconomic policy measures (adopted in the framework of export-oriented trade policy reforms introduced by developing countries since the 1980s) on the position of the small-scale sector vis-à-vis international trade.

A. Implications of trade policy reforms for the small-scale sector

31. Any assessment of the impact of trade reforms on the small-scale sector is hampered by the lack of statistical data and by analytical difficulties. First, markets are often not very well developed in many developing countries, with persisting distortions and market segmentations. Second, a large part of the small-scale sector is often not well integrated into formal markets. Third, by definition, the informal sector operates outside the officially recognized formal legal, fiscal and institutional frameworks. For these reasons, therefore, market signals and **government policies** may probably **not affect** the small-scale and, in particular, the **informal sector directly**. The indirect effects of macropolicies on informal enterprises can work through (i) the interaction with economic operators in the formal sector, and (ii) the policies that were not originally targeted to this sector.[14] For these reasons the expected positive results of national macroeconomic policy measures may never materialize.

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[13] See W. Elkan, *op.cit.*.

[14] For example, in many African countries, scrap metal used by small metalworkers consists largely of fragments of steel left from large-scale formal enterprises. Thus, in case where imports of steel are curtailed following adjustments in the exchange rate, informal enterprises can face serious bottlenecks in the supply of scrap metal.

1. Exchange rate policy reform

32. **Real devaluations** have helped in many cases to eliminate overvaluation-related distortions and the bias against exports and small, labour-intensive enterprises. On the side of imports, devaluations raise the domestic price of imported products. This may have twofold consequences for the small-scale sector. On the one hand, the higher price of imported goods puts them out of the reach of a number of customers and may consequently lead to a shift of demand towards domestically produced and cheaper substitutes (indirect impact of devaluation). This is especially true when the small-scale sector production is based on locally available inputs. The substitution effect should encourage firms with high proportions of domestic input, generally to be found among smaller enterprises. For example, evidence from Ghana suggests that recent devaluations have boosted the demand for small-firm products and have encouraged them to enter new product lines.[15/]

33. On the other hand, however, prices of both new and second-hand machinery imported from abroad tend to rise, hampering technological progress in the small-scale sector. In the case of a dependence on imported inputs, small enterprises may see their competitiveness falling on both the domestic and international markets (even though they are likely to be less affected than large, more import-dependent enterprises). In United Republic of Tanzania, for instance, the incentives to domestic exporters resulting from the 70 per cent devaluation from 1987 to 1990 were rapidly offset by the escalating cost of essential imports.[16/]

34. The second effect of devaluation works through a positive impact on exports. Domestic goods may gain a competitive edge in international markets and give a strong impetus to exports, including those originating from small production units. However, devaluations that do not reflect fundamentals might be difficult to justify or maintain in a highly competitive and managed international trading system.[17/]

2. Trade liberalization

35. The evidence concerning the impact of trade liberalization on the small-scale sector is scarce since little or no attention has been paid to the size of enterprises when considering trade liberalization issues. An attempt at drawing some conclusions can nevertheless be made. Some studies[18/] do show that trade liberalization measures (both in export regimes and in exchange rates) have

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[15/] See, T. Tesfachew: "Government policies and the urban informal sector in Africa", Working Paper, *World Employment Programme Research*, ILO, Geneva,1992, p.11.

[16/] "Tanzania: Difficult road of reform", *Africa Recovery*, vol.4, No 2, United Nations Department of Public Information.

[17/] For example, under-valuation of the currency may be considered as a form of dumping.

[18/] For example, V. Thomas, J. Nash and Associates, *Best Practices in Trade Policy Reform* (Oxford University Press for the World Bank, 1991); or J.N.Bhagwati, *Anatomy and Consequences of Export Control Regimes* (Cambridge, Ma., Ballinger Publishing Co., 1978).

generally encouraged export performance. Export booms have been mostly based on exports of manufactures growing at rates exceeding those of the export sector as a whole. As labour-intensive items form a considerable part of developing countries' exports it can reasonably be assumed that trade liberalization can be beneficial to small-scale enterprises engaged in export activities.

36. On the import-competing side, the implications do not seem to be so clear cut. The main losers have evidently been the large-scale enterprises confronted with increasing competition from imported goods resulting from the removal of protection. Some small-scale sector enterprises engaged in the production of import-substituting goods may also have been adversely affected by increased competition from abroad, particularly in the case of consumer goods. There is some evidence,[19/] however, to indicate that import competition is largely a problem for big firms, since small ones see other local small firms as their primary source of competition. At the same time, lower tariffs should reduce the prices of imported inputs, including capital equipment used by small and micro-enterprises. The elimination of quantitative restrictions should also widen access to imports beyond the large-scale firms that are usually favoured by the import licensing system.

37. It has been argued that trade reforms would have generally positive effects on employment in the small-scale sector for two reasons. First, a pattern of production in line with a country's comparative advantage would result in a higher share of relatively labour-intensive goods in total output. Second, the relative price of labour-to-capital would adjust to market levels and, if the labour supply was abundant, give incentives to the employment of more labour-intensive techniques.[20/] Since the labour-intensive goods produced by the small-scale sector would be more competitive and could sell better in international markets, the demand for labour should rise, especially for the unskilled workers who prevail among the poor, in order to increase exportable output. In Malaysia, for instance, export policies have induced a significant expansion of employment in labour-intensive manufacturing sectors such as textiles, industrial machinery and parts and assembly-based electronics. In Morocco, increased exports of textiles, clothing and leather products[21/] have given rise to additional employment creation which has been concentrated in small formal sector businesses.

38. On the other hand, however, trade liberalization could favour even more the larger enterprises that are able to benefit from economies of scale. In this case, the small-scale sector - despite its low labour costs - might not be able to compete because of low productivity. This argument applies in particular to the production of standardized goods where economies of scale are important. Handicrafts would be less vulnerable.

19/ See, World Bank, *Small Enterprises in Ghana: Responses to Adjustment* (Washington, D.C., 1990).

20/ See, G.T. Renshaw, "Market liberalization, equity and development", ILO, Geneva, 1989, pp.118 and 124.

21/ See, F. Bourguignon and Ch. Morrisson, *External Trade and Income Distribution* (OECD, Paris 1989), p.117.

B. Relevance of export promotion measures to the small-scale sector

39. It is recognized that although sound macroeconomic policies and trade liberalization eliminate anti-export bias, they are not a *sine qua non* for efficient export expansion by the small-scale sector. However, it is argued that policies that aim at creating a neutral environment for the choice between production for the domestic market and for exports might not by themselves bring about export expansion. Measures biased in favour of exports have therefore often been suggested. These include access to imported inputs at international prices, export subsidies, better access to finance for exports and improved infrastructure for exports.

40. Traditional export promotion measures are unlikely to have any direct impact on informal sector enterprises, since most of this sector is not eligible for government export incentives. The small-scale sector may, however, benefit indirectly if formal intermediaries use the benefits related to government export schemes to encourage their informal suppliers.

41. Small formal enterprises in most developing countries are in principle entitled to apply for concessions provided by export promotion schemes. The difficulty is, however, that regulations and administrative costs governing export incentives are often designed in such a way that the benefit accrues mainly to large enterprises. Moreover, the lack of information on credit facilities available in this area to small units may preclude small enterprises from making better use of government export promotion programmes.

42. It should be kept in mind that in most cases policy instruments have been generally designed to promote exports as a whole and rarely take into account the specific needs of the small-scale sector. Hence, further measures are needed to target government export promotion policies explicitly towards the small-scale sector.

III. TARGETED MEASURES TO SUPPORT THE SMALL-SCALE SECTOR IN INTERNATIONAL TRADE

43. The small-scale sector has for a long time been perceived as lacking export potential. The output of micro- and small enterprises was generally conceived to be of low quality and attractive only to a highly localized segment of the domestic market and to tourists in the case of handicrafts. For this reason, State support to exports has tended to concentrate on "prospective" large enterprises and hardly any attention has been paid to small businesses. Government-sponsored programmes (provided by various small and medium-sized enterprise development agencies[22]) for small-scale activities were therefore restricted to general support measures, without a link to exports.[23] At the same time, export promotion bodies established to develop the capacity of national enterprises specifically for exports have not paid special attention to the small-scale sector.

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[22] Assistance is rarely centred on a particular segment of the small-scale sector (with the exception of handicrafts development agencies).

[23] However, there are also countries that have been implementing long-lasting programmes of small-scale sector promotion in exports (such as Morocco, Tunisia and some countries in South-East Asia).

44. As a result of the growing awareness of the existence of untapped export potential in this sector, export promotion has become a part of the small and medium-scale enterprise development package.[24]

45. With the above in mind, State support should (a) extend concessional financial assistance to export activities, and (b) strengthen the export marketing capability within the small-scale sector. It is recognized, however, that the small-scale sector and micro-enterprises will have to bear the major responsibility for generating exports.[25] A role would also be played by foreign customers.

A. Improving access to export finance

46. A major hurdle for the small-scale sector is access to finance. The financial services that are available are usually oriented towards the large-scale sector, so that even small formal enterprises have difficulty obtaining credit. Informal enterprises do not have direct access to the banking sector and rely mainly on money lenders and other informal sources for financing, often at much higher cost.

47. In this context, special measures (*inter alia*, those discussed below) may be considered not only by governments but also by external agencies to ease the export credit constraint, either directly or indirectly. First, the activity of government agencies acting as intermediaries should be encouraged, as well as that of export houses selling the small-scale sector's output in foreign markets. Access for these intermediaries to bank advances would be helpful to facilitate exports as the money could be channelled through them to the small-scale sector.

48. Second, the requirement for collateral by financial institutions could be replaced by the provision of government-supported guarantees or insurance. For this purpose, pre-shipment export finance guarantee schemes could be introduced by governments to replace physical collateral. For example, the Korea Credit Guarantee Schemes and the Export-Import Bank of Korea provide this type of

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[24] In this context, specialized agencies to promote exports of small and micro-enterprises have been established in some developing countries (China, Colombia, Ghana, Guatemala, India, Indonesia, Lao People's Democratic Republic, Nepal, Pakistan, Philippines, Somalia, Thailand, United Republic of Tanzania, Viet Nam and Zambia); their records vary, however. The packages of assistance to develop export-oriented small-scale sector enterprises are sometimes offered by existing small and medium-sized enterprise development agencies or export development agencies as well. In some cases, both of them work together to encourage small enterprises to export.

[25] An example of growing awareness of this fact is the creation by small producers of a wide range of **sectoral and business associations**, mostly found within industrial clusters. Such associations provide members with various services (which may be alternatively offered by State agencies) aimed at raising the sector's competitive edge in international markets and ranging from consultancy to the creation of export consortia or technical centres for quality control. Sectoral associations seem to be very efficient in Latin America or Cyprus, for example, but their range of activities covers only small modern enterprises producing standardized goods (garments, footwear, furniture, etc.) and apparently have no direct links to the informal sector.

guarantee.[26] In Chile, small producers of non-traditional exports can obtain a guarantee from the Guarantee Fund for Non-Traditional Exports for loans covering working capital requirements.[27] At the subcontractor level, simple procedures for obtaining bank loans using purchase orders or letters of credit as collateral could be helpful to small enterprises. At the artisan level, NGOs, cooperatives and rural banks, as well as commercial banks, could be encouraged to provide small credits by using innovative forms of guarantee such as, for example, collective responsibility.

49. Third, in order to strengthen the small-scale sector's competitiveness in export markets and its capacity to offer attractive terms to importers, it would help to provide pre- and post-shipment export finance on concessional terms. In India, for example, subsidized credit is in principle available for most exporters of manufactures, including small producers. In addition to pre- and post-shipment credit, small producers can also obtain subsidized bank loans for working capital. For handicrafts such as carpets, gems and jewellery, these loans may be equal to as much as half the value of the export order, at an interest rate of 3 to 5 percentage points below the prime lending rate. The problem is, however, that many exporters are considered by the banks to be too small or too risky and are therefore excluded from the scheme.[28]

B. Identifying exportable products

50. It is generally accepted that developing countries have a competitive advantage in labour-intensive production. Because of the relatively high costs of labour in the OECD countries, and rising wages in newly industrialized economies, a window of opportunity exists for low-labour-cost developing countries to enter international markets in the production of labour-intensive products. Niche markets for these countries exist, for instance, as we have seen, in specialized garments, leather-based goods, wood and rubber-based products, hand-made jewellery, electronics, precious stones and fruit juices.

51. The capability to fill niches in international markets is partly determined by technological developments, as consumers' preference is shifting towards quality rather than price. Within the technological choice, a question is whether the use of labour-intensive techniques in small enterprises is economically well-founded or whether more capital-intensive technologies are inevitable once enterprises export to more demanding markets. It seems that efforts to move up-market are increasing the demand for modern equipment, opening up job opportunities for higher-qualified installation and maintenance personnel, and therefore creating fewer jobs for poor and unskilled workers. Apart from subcontracting arrangements, such trends also imply a diminished role in exports for the small-scale sector, given the economies of scale inherent in larger enterprises.

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[26] International Trade Centre UNCTAD/GATT, *Exports from Small and Medium Enterprises in Developing Countries: Issues and Perspectives* (Geneva, 1989), p.131.

[27] See, L. Henríquez Amestoy: "Chile - experiencia exportadora de las impresas pequenas y medianas", *Comercio exterior*, No.6, June 1993, p.549.

[28] See, V. Cable, A. Weston and L.C. Jain, "The commerce of culture - Experience of Indian handicrafts", *Lancer International*, New Delhi,1986, p.209.

52. Concern has been expressed that labour-intensive technologies may be too inefficient and cannot meet the quality requirements of importers, thus making it difficult to compete in international markets. Studies carried out by the ILO[29] conclude, however, that some technologies requiring high labour inputs are cheaper than capital-intensive alternatives, while being efficient and producing goods of adequate quality. Both the objective of competitiveness and that of employment creation can be achieved with the use of such technologies.

53. However, there are factors that impede a broader proliferation of these labour-intensive yet efficient technologies. These include: (a) lack of information about possible technological choices, (b) misconceptions about labour-based methods, based on the belief that modern, capital-intensive techniques are the only means of improving quality and efficiency, and (c) lack of attention in research and development in developing countries to the development of suitable labour-intensive technologies. Technological change aiming at greater efficiency (and employment creation) ought therefore to be promoted to the utmost extent possible.

54. One possibility is to try to upgrade traditional technologies that are no longer efficient or competitive.[30] Another is to promote research on alternative-employment-creating competitive technologies. Thirdly, it would help to improve the access of small enterprises to information about appropriate labour-intensive technologies in use in other parts of the world.

55. Labour-intensive technologies, however, cannot be advocated as a solution *per se*. They may often be unsuitable when goods are being made for an export market that requires a large volume of items of consistent quality within a short time-frame. In these situations, it may be necessary to import modern technologies in order to reduce costs and to achieve international standards of quality. As far as standardized labour-intensive production is concerned, the necessary technology is sometimes provided or suggested by foreign investors, which often supply technical assistance in quality control and in training personnel. This may be one of the reasons why modern small industries in developing countries are sometimes as capital intensive as larger manufacturers. By contrast, more labour-intensive technologies continue to prevail in handicrafts sectors where specific skills are not as easy to substitute for machines.

C. Placing products on foreign markets

56. The search for foreign markets for small-enterprise production is a complex task requiring a systematic and professional approach to export marketing. The issue is somewhat different in the case of standardized manufactured products and in the case of more "personalized" handicrafts items. Most manufactured products have established markets and a new producer has, in a sense, merely to produce these goods in the required quality and price according to the importer's specifications. It is also true that trade-creating initiatives often come from developed country partners or their agents seeking low-cost suppliers.

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[29] Summarized in ILO, *Technologies Which Are Appropriate for Meeting Social Objectives of Developing Countries*, Geneva, 1985.

[30] However, not all traditional technologies can be upgraded and, as a matter of fact, their use lowers the competitiveness and marketability of products.

Understanding and being able to satisfy importers' needs and requirements may be sufficient for successful exporting in such cases.

57. The situation is much more difficult for **handicrafts**, which face fierce competition in limited international markets. The basic strategy for handicraft exports must therefore start by fostering demand, i.e. **markets must be created**[11] in developed countries for a particular handicraft item. The initial stages of market creation are generally beyond the capabilities of micro- and small producers and export houses due to their lack of individual influence and difficulty in attracting the attention and collaboration of foreign partners. In these early stages, leadership and financial support might come from government agencies.

58. Small producers can hardly be expected to carry out export functions by themselves. The question that then arises is how to get the product to export markets. Three **main models of distribution channels**, including varying numbers of intermediaries (whose involvement is absolutely vital for the participation of micro-enterprises in international trade), are described below.

Table 4

Typology of distribution channels

First model: *from* - Producer	to - (Buyer's agent/representative)* (in the developing country)*		to - Foreign buyer
Second model: from - Producer	to - Intermediaries	to - Export house	to - Foreign buyer
Third model: from - Producer	to - Large domestic or foreign manufacturer, based in the developing country	to - (Export house)*	to - Foreign buyer

* Brackets indicate that this particular element of the chain may be omitted.

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[11] A "product push" marketing strategy might be preferable in the case of handicrafts. The objective would be to persuade distribution channels that handle large volumes, or are influential in the trade (e.g. mass merchandisers, large importers, influential fashion leaders, opinion makers), to carry the handicraft concerned as one of their product lines. An example that can be given is the association of the House of Pierre Cardin with the promotion of Indian hand-loomed goods on European markets. Many hitherto unknown items from India became popular, bringing about a rise in exports. It should be noted, however, that fairly large investments are required to identify trading partners and gain their cooperation, with no assurance of success. See, International Trade Centre UNCTAD/GATT, *Handicrafts and Cottage Industries: A Guide to Export Marketing for Developing Countries*, Geneva, 1991, p.28.

59. **The first model** applies generally to standardized manufactured products and small formal enterprises where direct or nearly direct contact (through a buyer's agent) may be established. Both parties prefer a mutually advantageous long-term collaborative relationship. The buyer can thus build a reliable low-cost source of supplies whereas the producer is generally incorporated in an industry network through which he can acquire production and marketing information and assistance to upgrade quality and skills and to cut costs. The goods are then sold under foreign brand names.

60. Three main types of buyers can be distinguished in business relations of this kind. First, large retailers (department stores or independent retailer buying groups), which buy finished products directly from foreign manufacturers and often maintain networks of international representatives both to seek out potential suppliers and to maintain overseas buying offices. It is estimated that about 20 per cent (more than 50 per cent for garments and textiles) of developing countries' manufactures are exported through buying offices of large retailers.[32/] Second, importers-wholesalers, which buy from foreign manufacturers for resale either to domestic retailers or to other intermediaries. A large proportion of trade in handicrafts thus passes through importers, which have usually specialized in a particular product range (basketry, carpets etc.). Third, manufacturers in the same line of products, which buy finished goods or components from foreign manufacturers. The proportion of goods imported directly by manufacturers may well exceed the amount accounted for by retailers' buying offices.

61. **The second model** is more complex and serves mainly dispersed artisans and cottage-industry workers. Clearly, these informal producers would not be in a position to organize their production single handed, nor, in general, could they gain access to markets on their own, much less export directly. For these reasons, between the large number of primary producers and the export houses there are one or more layers of intermediaries which perform a range of production and marketing functions for small producers (providing raw materials, dyes, colours and designs, and buying products for resale to exporters). In most countries these intermediaries are perceived as "rent-seekers", since they tend to extract maximum profit from each transaction, leaving the producer little incentive for development and thereby stifling the spirit of enterprise and ultimately the enterprise itself. In this context, an interesting initiative has been undertaken in Sri Lanka, with strong support from the Government, to build up an alternative intermediary in the form of the Export Production Village Company, to take care of the management, financing and marketing of rural producers' exports.[33/] A similar objective has been pursued through the organization of small producers into cooperatives (with a highly variable record of success, however), or through a government agency's involvement in the organizational part of the task.

62. In the above example, intermediaries then supply the products to export houses. These do not usually engage in production, but instead handle the export

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32/ See, M. L. Egan and A. Mody: "Buyer-seller links in export development", *World Development*, No.3/1992, p.322.

33/ For details, see International Trade Centre UNCTAD/GATT, *Export Production Villages: A Study of a Sri Lankan Scheme for Rural Export Development*, Geneva, 1992.

of a wide variety of products on the basis of export licences issued by the government. In many countries, State-sponsored agencies such as handicraft corporations perform the commercial function of an export house, in addition to carrying out a developmental role, although also with varying success.[34] The advantage of large export trading houses in general is that they have greater bargaining power vis-à-vis importers and are better able to negotiate conditions of sale with them than smaller operators.

63. **The third model** is in fact a subcontracting arrangement between a micro- or small enterprise and a larger manufacturer. The first form of subcontracting consists of the physical incorporation of small unit-generated semi-processed goods, components or subassemblies in exports by larger (domestic, foreign or multinational) manufacturers.[35] In the case of local manufacturers, specialized exporters may be used for export purposes, whereas transnational corporations and their subsidiaries export without going through intermediaries. The second frequent option for large manufacturers is to contract out the most labour-intensive operations involved in products for export to enterprises in the small-scale sector, which are often of an informal nature.[36]

D. Providing know-how for international business

64. It is generally recognized that exporting is much more difficult than selling to the domestic market in terms of the knowledge and skills required. Exporting requires expertise in export marketing in addition to the ability to produce an exportable product. There is a need for personnel with the skills, knowledge and confidence to initiate and develop the export function.

65. In this context, three types of training scheme are important for economic agents in the export business. First, small enterprises (and intermediaries) would benefit from highly practical managerial training modules covering such topics as: how to start a small business; how to arrange for the financing of a small business; how to hire personnel; how to take advantage of government incentives; and how to maintain quality control of raw materials, work stations and final products. The level of sophistication of the training would vary according to the education levels of the trainees. Second, a module on export

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[34] The Hand-loom and Handicrafts Export Organization of India may be cited. It operates showrooms and retail outlets abroad, assists in the development or procurement of designs and is committed to the success of the supplier and product. See, International Trade Centre UNCTAD/GATT, Handicrafts and Cottage Industries ...", *op.cit.*, Geneva, 1991, p.17.

[35] In India, for example, the local affiliate of Philips has been operating a "Partners in Progress" programme, with 1,600 small-scale suppliers, in total employing some 60,000 people. The units receive a wide range of assistance in finance, management, product development, training, etc. See, D. L. Wright: "A Study of the Employment Effects and Other Benefits of Collaboration between Multinational Enterprises and Small-scale Enterprises", Working Paper No.60, ILO, 1990, pp.7-8.

[36] An example is the Bata Shoe Company of Ceylon Ltd., which has a subcontracting system for some operations in the production of shoes (e.g. stitching of uppers, covering of insoles), with approximately 80 sub-contractors and 1,300 people involved. National Seminar on Small Enterprise Development Opportunities in Sri Lanka, *Background Papers*, 20-22 September 1989, p.220.

marketing designed for export houses (and intermediaries) would be useful in covering export procedures, packaging requirements, costing and pricing for exports, market selection, product improvement and sources of assistance. Third, as export-promoting and small and medium-sized enterprise-developing agencies are often responsible for designing, coordinating and supporting these programmes, it would help if the relevant capabilities of their staff were built up. Personnel from these agencies, whether they be governmental or non-governmental, should be trained in the organization (and provision) of marketing activities, and in the counselling of enterprises on exporting. Moreover, all staff coming into contact with foreign partners ought to have have at least a working knowledge of a major foreign language.

66. It is widely accepted that a good level of general education (literacy and numeracy: the three "Rs") is essential if a country aspires to have a competitive workforce in today's global economy. Governments should therefore emphasize access to general education, in particular, for the poorer segments of society, and seek to improve its quality.

IV. POLICIES TO IMPROVE ACCESS TO DEVELOPED COUNTRY MARKETS FOR LABOUR-INTENSIVE PRODUCTS FROM DEVELOPING COUNTRIES

67. The key to the success of export-led growth strategies in terms of employment creation lies only partly in the hands of domestic policy-makers and internal factors in the developing countries. Labour-intensive production in small enterprises may be stimulated through targeted policy measures, but those will only lead to the expected growth in employment if the goods find markets.

68. Concerns about employment in many developed countries have long translated themselves into a growing interest in social issues, and into various forms of protectionism against labour-intensive imports from developing countries. Developed countries' trade policy vis-à-vis developing countries has always tended to be more restrictive in the sectors where both groups of countries compete. Tariff concessions often tend to be lower, and non-tariff barriers higher, for developing countries' exports of agricultural items and for labour-intensive manufactured products for which developed countries have lost their competitive edge. In this respect, the export possibilities of the small-scale sector are often affected since their products are usually relatively labour-intensive. Two main groups of market access barriers may be identified: tariffs and non-tariff measures.

69. **Tariffs** are generally recognized to have lost much of their import-restricting power as a result of trade liberalization measures. However, there are still areas where they have an important impact on trade flows, including labour-intensive trade which affects small-scale and micro-enterprises. Even if around 50 per cent of developing countries' manufactured exports to the developed world are covered by the generalized system of preferences (GSP), of which about 50 per cent are actually granted GSP treatment,[37] labour-intensive items have generally received less favourable treatment. The elements that have

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[37] For details see, for example, UNCTAD, "Seventeenth general report on the implementation of the generalized system of preferences: Recent changes and policy issues" (TD/B/SCP/6), 1994.

discriminated against them can be identified both within most-favoured-nation (MFN) rates and within the GSP.

70. First, **labour-intensive items** have **frequently not been included in the GSP schemes** at all, or only to a limited extent (e.g. tariff quotas or ceilings). In textiles and clothing, for example, only 71 per cent of tariff lines were covered by the GSP in the 1980s, the average for all industrial sectors being 90 per cent.[*] In the United States of America, textiles and textile products have not generally fallen under the GSP at all; in the European Community tariff concessions for the same group of products have been granted only to parties to the Multi-fibre Arrangement (MFA) that have bilateral agreements with the European Community up to specific amounts under MFA quotas; and for Japan GSP ceilings have been introduced.

71. Labour-intensive handicrafts and handmade products which are produced, in particular, by the small-scale sector have also been offered preferential treatment under special provisions for handicrafts and handmade items granted by the major developed countries, both within and outside the GSP. However, the coverage of textiles has been restricted even under these schemes and the use of tariff quotas has been rather frequent.

72. Consequently, higher MFN tariffs have often been imposed on imports of non-eligible goods, either totally or after exceeding tariff ceilings. In general, **labour-intensive products have faced much higher MFN tariff rates.** In this context, the extension of the product coverage of GSP schemes (including food products), the elimination of tariff ceilings and deeper cuts in MFN rates for high-tariff items may be instrumental.

73. Moreover, despite the calls for diversification of developing countries' exports from primary commodities to semi-finished goods and manufactures, the structure of MFN tariffs in developed countries has restrained this objective. In fact, the degree of protection has increased with the advance up the production chain towards higher value-added products (tariff escalation). In principle, two ways of eliminating the bias against processed products might be envisaged: one might be to negotiate a flat tariff structure with the same tariff rate applied throughout the processing chain; while the second might be to include processed products in the GSP, with a zero or very low tariff rate.

74. **Complex rules of origin and** other **administrative procedures** that have to be complied with before a country is entitled to GSP treatment should be simplified as well.

75. In the context of the results of the Uruguay Round, concerns about the direct impact in the case of further cuts in MFN rates are being expressed by developing countries, in relation to the possible **erosion** of present **preferential margins.** The hardest hit will be the least developed countries and the African, Caribbean and Pacific (ACP) countries which, at present, export mostly duty free or under very low tariffs to the developed countries. Compensatory policies for adoption by the preference-giving countries are therefore being requested.

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[*] See, V. Cable, "Textiles and clothing in a new round of trade negotiations", *The World Bank Economic Review*, No.4/1987, p.640.

76. Protectionism has increased over the years in the developed countries in response to the export challenge posed by the developing world, bringing about frequent discretionary interventions and the use of progressively more subtle forms of **non-tariff barriers** against manufactured exports, particularly those that are labour intensive from competitive developing countries. Among the main non-tariff measures, there have been variable levies, the restrictions under the Multi-fibre Arrangement,[39] global and bilateral quotas, voluntary export restraints (VERs), restrictive licensing systems, the protectionist use of antidumping and countervailing duties, and price undertakings. Protection has been applied on an industry-specific basis, i.e. selectively in those industries that have experienced major economic problems. Its application has been justified by the industries' need of a sufficient period in which to adjust their production to the new challenges. Such protection has been viewed as a temporary measure, to be phased out as the domestic industry restructures itself.

77. The ideal would be a greater awareness of the importance of **interdependence**. An increase in the South's exports would raise incomes in the South and also ease balance-of-payments problems, both of which would also lead to an increase in the South's purchases from the North. This feedback effect would not only contribute directly to the North's employment in export industries, but also, through secondary or multiplier effects, help to increase the North's growth rate, thus creating further employment.[40]

ISSUES FOR DISCUSSION

Based on the foregoing, therefore, certain issues are open to debate, as follows:

(1) According to country experiences, what types of small and micro-enterprises have proved to be the most successful in exports? What are the main reasons for their success?

(2) Are the successful exporting enterprises also employment creating, i.e. using labour-intensive technologies, or do they mostly tend to substitute capital for labour? Is there a rationale for policies favouring higher labour intensity, despite the possible conflict with efficiency objectives?

(3) What are the competitive advantages in exports of small-scale enterprises that are capital intensive, given that they do not have the economies of scale of large enterprises ?

(4) What products, or types of products, originating from the small-scale sector are particularly competitive in the developed markets in terms of

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[39] The Final Act of the Uruguay Round stipulates a progressive abrogation of the Multi-fibre Arrangement within a 10-year period.

[40] In fact, in 1990-1991 developing countries absorbed 19.3 per cent of developed countries' exports. The most important employment creation has occurred in higher value-added industries such as specific base chemicals and plastics, non-electrical, electrical and transport equipment and professional and scientific goods, where the dependence on exports to developing countries oscillates between 30 and 80 per cent of total sectoral exports from developed countries.

their marketability and the capacity to fill existing market niches?

(5) Have trade policy reforms, many of them corresponding to structural adjustment programmes, been generally beneficial or detrimental to the small-scale sector: (a) in terms of its export performance , (b) in terms of the impact on the sector of liberalized imports from abroad?

(6) What lessons can be drawn from country experiences related to the targeted promotion of small and micro-enterprises in international trade? What measures can be suggested to improve the efficiency of government assistance to the small-scale sector's exports?

(7) What types of trade barriers have been the most restrictive vis-à-vis the small-scale sector exports to the developed markets? Bearing in mind the conclusions of the Uruguay Pound, what policies should be pursued to mitigate their impact and to facilitate the access of labour-intensive products from developing to developed countries?

Annex

SELECTED PRODUCT-RELATED ISSUES RELEVANT TO THE PROMOTION OF EXPORTS BY SMALL AND MICRO-ENTERPRISES

1. Product-related aspects are becoming increasingly important to the success of exports, particularly for small enterprises. In this context, a **low price** is no longer a sufficient prerequisite for export success in developed markets. Even for the lowest-cost products within a product segment, there are minimum product criteria, including not only a competitive price but also a corresponding quality, packaging and on-time delivery.

2. **Quality requirements** exist for every product niche - whether or not the product is high-priced. If the quality of the product does not meet defined standards (which will vary according to the price categories of products) the product will not be marketable, regardless of its price or punctual delivery.

3. Two options must therefore be simultaneously pursued in order to improve the competitiveness of small enterprises in terms of quality of output. First, given the frequent failure of producers to regulate the quality of many items, and especially handicrafts, there is an argument for the introduction of **some form of quality control** by government authorities, based on defined minimum standards. For example, for certain items, governments could seek to implement internationally recognized standards, preferably based on the quality system defined by the International Organization for Standardization (ISO). Compliance with these standards would be perceived as giving a product a guarantee of worldwide credibility. In the case of exports of food products, results of microbiological tests may be required by the customer, and compliance with the importing country's standards (for example, concerning the contents and quantities of certain substances in food) may be indispensable.

4. To ensure the implementation and administration of quality standard systems, institutions and/or the establishment of services related to quality control and standards should be built up, with public support, at an international level. An example would be that of India: the Export Inspection Council is in charge of pre-shipment inspection, wherein, for example, handloom items are inspected before they are given "India item" certificates.[41/] However, such institutions, in particular in developing countries, are often plagued by problems of inefficiency and delay, and their ability to provide assistance is limited. This is one of the reasons why buyers from developed countries often prefer to send certain products to their home countries for testing. It might, therefore, sometimes be preferable to pursue certification strategies by forming links with standards and certification institutions in developed nations, as they can often provide greater credibility.

5. Second, an alternative would be for governments to require or encourage manufacturers and exporters to **impose a degree of self-control through professional associations**. The producers themselves would seek to change the workplace culture and attitudes of personnel to quality and responsibility by inducing greater awareness of the importance of quality, as well as through the improvment of work skills. Efforts to achieve a higher level of quality could be stressed, for example, in a general campaign, both by government bodies, producers' associations and export agencies. Awards for the attainment of quality could be given. Permission to use an exclusive mark of distinction (developed with financial support from the government), when the goods passed certain tests for standards, could also help to encourage the production of higher quality items. Useful technical cooperation in quality issues can be provided by customers from developed countries as well.

6. **Packaging** frequently affects both the importer's and consumer's perception of the overall quality of goods. Moreover, "packaging is a silent salesman" and

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41/ See, V. Cable, A. Weston and L.C. Jain, *op.cit.*, p.201.

has an important information function to impart. This is true especially of handicraft items which are sold as gifts and must frequently compete with various manufactured products from developed countries presented in sophisticated promotional gift packages. The increase in costs related to more attractive and competitive packaging may be offset by sales at better prices.

7. The current packaging of goods used by developing countries still quite often falls short of the requirements on highly competitive markets in the industrialized world. This is true from both a purely technical point of view (i.e. protection provided, structural design) and from a promotional point of view (graphics, sales appeal). It is therefore important to convince all those involved - government officials, trade promotion organizations, producers and exporters - of the need for technically adequate and sales-effective export packaging.

8. Because of the cost and related technical aspects, packaging for export markets may well be beyond the capabilities of most micro-enterprises. This implies that there is room for initiatives to improve export packaging, which should originate from export houses, possibly in cooperation with the government agency responsible for the development of the small-scale sector. Where enterprises are unable to cope with packaging requirements, a common packaging assistance centre could be established, with the financial participation of the government in the initial investment stages.

9. **On-time delivery** is an equally important criterion for suppliers. Goods must be delivered within the time-frame agreed, and orders must be complete. The importance of on-time delivery stems from the need to meet customers' manufacturing production schedules, as well as, for example, fashion cycles and seasonal sales peaks. The producers should be aware of this, as well as of the fact that delays in delivery may mean losses for them too, if the customer claims damages due to non-observance of the delivery date, or future orders are jeopardized.

10. Even if the product's price, quality and delivery dates do meet international standards, this does not imply that the product will necessarily sell well in foreign markets. The reason of course may be quite simple - the product does not correspond to the tastes and preferences of customers in other countries. This may be especially true in the case of fashion articles or handicrafts where the design or cut are particularly important aspects. **Product development or adaptation** is therefore often necessary to make the product marketable in developed countries. For standardized products, which do not bear the marks of their country of origin, the designs can be provided by the importers, without the participation of local designers. By contrast, however, in the case of handicrafts, contemporary designs could be created that utilize the basic distinctive features of the traditional articles but at the same time make the product acceptable to import markets. The necessary impetus or help is frequently provided by the importing market, but it is equally important to establish a domestic capability for initiating design. Training programmes to prepare qualified domestic designers, at least for the sectors with high export potential, could help in this regard and should therefore be encouraged.

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Quality of analysis, including objectivity	☐	☐	☐	☐	☐
Validity of conclusions	☐	☐	☐	☐	☐
Clarity of recommendations	☐	☐	☐	☐	☐
Comprehensiveness of coverage	☐	☐	☐	☐	☐

7. **If you have any other observations or comments please use the back of this sheet.**

_____

_____

_____

Finally, we would appreciate your providing the following information about yourself:

Area of work: _____
(e.g. governmental, private enterprise, academic institutions)

Functional title: _____

Name and address: _____
(Optional)

Thank you for you co-operation.

Please forward the questionnaire to:

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